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Nos. 84-871, 84-889, 84-1054, and 84-1069

In the Supreme Court of the United States

OCTOBER TERM, 1984

Louisiana Public Service Commission, Appellant
v.
Federal Communications Commission and
United States of America

California and Public Utilities Commission
of California, et al., Petitioners
v.
Federal Communications Commission and
United States of America

Public Utilities Commission of Ohio,
et al., Petitioners
v.
Federal Communications Commission and
United States of America

Florida Public Service Commission, Petitioner
v.
Federal Communications Commission and
United States of America

On Appeal And On Petitions For A Writ Of
Certiorari To The United States Court Of Appeals
For The Fourth Circuit

BRIEF OF APPELLANT, THE LOUISIANA PUBLIC SERVICE COMMISSION, AND PETITIONERS, THE PUBLIC UTILITIES COMMISSION OF OHIO, THE OHIO OFFICE OF CONSUMERS' COUNSEL, AND THE FLORIDA PUBLIC SERVICE COMMISSION

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QUESTION PRESENTED

May the Federal Communications Commission order State regulatory agencies to increase intrastate rates to further a Federal policy allowing telephone companies faster capital recovery, although the Communications Act reserves jurisdiction over intrastate rates to the States?[1]

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[1] The Virginia State Corporation Commission was the petitioner in the proceeding before the court of appeals. The Federal Communications Commission and United States of America were respondents. The Louisiana Public Service Commission, Public Utilities Commission of Ohio, Office of Consumers' Counsel for the State of Ohio, and Florida Public Service Commission were intervenors supporting the petitioners. The following parties also supported the petitioner:

State of Michigan and Michigan Public Service Commission;
Department of Public Utility Control of the State of Connecticut;
People of the State of California and the Public Utilities Commission of the State of California;
National Association of Regulatory Utility Commissioners;
Public Service Commission of the District of Columbia;
Arkansas Public Service Commission;
Kansas State Corporation Commission;
Public Service Commission of Wyoming;
Washington Utilities and Transportation Commission;
Department of Public Service of the State of Minnesota;
Arizona Corporation Commission;
Citizens of the State of Florida;
National Association of State Utility Consumer Advocates;
Consumer Advocate of South Carolina;
Iowa State Commerce Commission;
Public Service Commission of Wisconsin;
Public Service Commission of West Virginia;
New York State Department of Public Service; and
Board of Public Utilities of New Jersey.

The intervenors supporting the respondents included:

North American Telephone Association;
American Telephone and Telegraph Company;
Southern Pacific Communications Company;
GTE Service Corporation;
Continental Telecom, Inc.;
United Telephone System, Inc.;
Cincinnati Bell, Inc.;
The Bell Telephone Company of Pennsylvania;
The Chesapeake and Potomac Telephone Company;
The Chesapeake and Potomac Telephone Company of Maryland;
The Chesapeake and Potomac Telephone Company of Virginia;
The Chesapeake and Potomac Telephone Company of West Virginia;
The Diamond State Telephone Company;
Illinois Bell Telephone Company;
Indiana Bell Telephone Company, Inc.;
Michigan Bell Telephone Company;
The Mountain States Telephone and Telegraph Company;
New England Telephone and Telegraph Company;
New Jersey Bell Telephone Company;
New York Telephone Company;
Northwestern Bell Telephone Company;
The Ohio Bell Telephone Company;
Pacific Northwest Bell Telephone Company;
The Pacific Telephone and Telegraph Company;
Bell Telephone Company of Nevada;
South Central Bell Telephone Company;
Southern Bell Telephone and Telegraph Company;
Southwestern Bell Telephone Company; and
Wisconsin Telephone Company.

STATEMENTS OF SUPPORT

The following parties in Docket No. 84-889 have authorized the parties sponsoring this brief to state that the listed parties support the positions advanced here as well as those contained in their own brief: National Association of Regulatory Utility Commissioners, Arkansas Public Service Commission, California and California Public Utilities Commission, Department of Public Utility Control of the State of Connecticut, Public Service Commission of the District of Colunbia, Public Counsel of the State of Florida, Iowa State Commerce Commission, Kansas State Corporation Commission, State of Michigan and Michigan Public Service Commission, Department of Public Service of the State of Minnesota, New York State Department of Public Service, South Carolina Consumer Advocate, Washington Utilities and Transportation Commission, Wisconsin Public Service Commission.

In addition, the parties sponsoring this brief support the positions advanced by the parties in Docket No. 84-889.

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The opinion of the court of appeals is reported as *Virginia State Corp. Com'n v. F.C.C.,* 737 F.2d 388 (4th Cir. 1984) (Jurisdictional Statement Appendix ("J. S. App.") at A-1 *et seq.*) This opinion affirmed a ruling of the Federal Communications Commission, which is reported as *Amend. of Part 31,* 92 F.C.C.2d 864 (1983) (J.S. App. at A-24 *et seq.*) The ruling overruled a previous decision of the Commission, reported as *Amend. of Part 31,* 89 F.C.C.2d 1094 (1982) (J.S. App. at A-61 *et seq.*)

JURISDICTION

The Jurisdictional Statement and Petitions for Writs of Certiorari review the relevant dates.[2] The appellate jurisdiction of the Court is invoked in No. 84-871 pursuant to 28 U.S.C. §1254(2); the certiorari jurisdiction is invoked in Nos. 84-889, 84-1054 and 84-1069 pursuant to 28 U.S.C. §1254(1).

The Court postponed the question of jurisdiction in No. 84-871 to the hearing of the case on the merits. That issue is addressed in Section II.

STATUTORY PROVISIONS

The following federal statutes, reprinted commencing at J.S. App. A-131, are involved in this case:

47 U.S.C. §151
47 U.S.C. §152
47 U.S.C. §153(e)
47 U.S.C. §220

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2 Jur. St., No. 84-871, at 3; Pet., No. 84-1054, at 1; Pet., No. 84-1069, at 2. *See also* J. S. App. at A-90 - A-93.

47 U.S.C. §221(b)
47 U.S.C. §221(c)
47 U.S.C. §410

Certain Louisiana State ratemaking orders were invalidated by the *Preemption Decision* of the Federal Communications Commission, as enforced in a Federal court injunction proceeding, and are set forth beginning at J.S. App. A-94.

STATEMENT OF THE CASE

Preliminary statement.

The issue is whether the Federal Communications Commission ("FCC") may require State regulatory commissions to increase intrastate telephone rates, despite express statutory provisions reserving jurisdiction over these rates to the States. The FCC preempted State ratemaking practices that were inconsistent with two of its own accounting orders[3] and mandated the adoption of the Federal procedures in setting intrastate rates.[4] The United States Court of Appeals for the Fourth Circuit affirmed the *Preemption Decision* by a 2-1 majority.[5]

The *Preemption Decision* discarded nearly 50 years

[3]*Amend. of Part* 31, 83 F.C.C.2d 267 (1980); *Amend. of Part 31*, 85 F.C.C.2d 818 (1981).

[4]*Amend. of Part 31*, 92 F.C.C.2d 864 (1983) (hereinafter cited as "*Preemption Decision*"), J. S. App. at A-24.

[5]*Virginia State Corp. Com'n v. F.C.C.*, 737 F.2d 388, 396 (4th Cir. 1984), J.S. App. at A-1, A-17.

of history, in which Federal and State regulatory responsibilities have been divided using a separations process pursuant to the Communications Act. It ordered that rates be increased for plant assigned to State regulation. To justify its action, the FCC characterized a reporting provision in the Communications Act as an authorization for intrastate ratemaking. To assist the Court in understanding the magnitude of the FCC action, this brief will review the regulatory context in which the *Preemption Decision* was issued.

1. Interstate-intrastate separations.

Since prior to passage of the Communications Act,[6] the interstate and intrastate plant and expenses of telephone carriers have been, and continue to be, divided for ratemaking purposes. Purely intrastate plant and expenses are assigned directly to the relevant intrastate jurisdiction.[7] Purely interstate plant and expenses are assigned to the interstate jurisdiction.[8] Jointly used plant and expenses — the investment and costs incurred to serve both interstate and intrastate purposes — are divided using separations factors. These factors are developed by Federal-State Joint Boards, composed of FCC members and representatives of State agencies.[9] The FCC sets interstate toll rates and interstate "access" charges to cover the expenses and provide a return on the investment

[6]*See Smith v. Illinois Bell Telephone Co.*, 282 U.S. 133 (1930).

[7]*See, e.g., 47 C.F.R.* §§67.124(b),(c),(d), 67.125(c), (d), 67.311(b) (1984).

[8]*See* regulations cited in n.7 *supra.*

[9]*See* 47 U.S.C. §410(c).

assigned to the interstate jurisdiction. The State agencies set intrastate rates and charges to cover intrastate expenses and provide a return to intrastate investment.

The separations process emanates from *Smith v. Illinois Bell Tel. Co.,*[10] where this Court mandated the separation of the intrastate and interstate plant and expenses of a telephone company in testing the fairness of an intrastate rate order. The Court ruled that "[t]he proper regulation of rates can be had only by maintaining the limits of state and federal jurisdiction . . . ."[11] It required a reasonable apportionment of the property of the company based on use.[12]

In the Communications Act of 1934, Congress recognized the need to separate the property of carriers for ratemaking. It provided that the FCC could classify the property used for interstate communications.[13] Subsequently, the FCC and State regulators cooperated to develop simple and equitable separations procedures.[14] In 1971, Congress passed the Federal-State Communications Joint Board Act, 47 U.S.C. §410(c), which memorializes procedures previously developed for making jurisdictional

[10]282 U.S 133 (1930).

[11]*Id.* at 149.

[12]*Id.* at 151.

[13]47 U.S.C. §221(c), J.S. App. at A-137.

[14]*See* the Senate Report on the 1971 Federal-State Communications Joint Board Act, enacted as 47 U.S.C. §410(c). S.Rep. No. 92-632, 92d Cong., 1st Sess., *reprinted in* 1971 U.S. Code Cong. & Ad. News 1511, 1512.

separations. Currently about 25 per cent of telephone plant is allocated to the interstate jurisdiction, and about 75 per cent remains in the intrastate jurisdictions.[15]

2. FCC Uniform System of Accounts.

Section 220 of the Communications Act authorizes the FCC to prescribe the form of accounts for certain telephone carriers and requires these carriers to maintain their records as prescribed by the FCC.[16] This section also gives authority to the FCC to prescribe depreciation practices.[17] These provisions permit the FCC to prescribe a uniform basis for *reporting* the financial affairs of carriers, for the benefit of investors, creditors, regulators, management and others.[18] The FCC uniform system of accounts has never been viewed as binding for ratemaking at either the Federal or State level.[19] State agencies often rely on the FCC uniform system, but carriers usually maintain separate intrastate records to accommodate intrastate ratemaking practices.

The purpose of uniform accounting is to require carriers to report their affairs on a comparable basis.[20] The

[15]*See Amend. of Part 67,* 96 F.C.C.2d 781, 785 n.11 (1983).

[16]47 U.S.C. §220(a), (g), J.S. App. at A-133 - A-136. "Connecting carriers" are defined in Section 2(b) (2) of the Act, which excludes them from all FCC regulation except pursuant to Sections 201-205.

[17]47 U.S.C. §220(b), J.S. App. at A-133 - A-134.

[18]*See, e.g., South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 352 So.2d 964, 981 (La. 1977), *cert. denied* 437 U.S. 911 (1978).

[19]*See Washington Pub. Int. Org. v. Public Serv. Com'n,* 393 A.2d 71, 79-82 (D.C. App. (1978), *cert. denied,* 444 U. S. 926 (1979).

[20]*See Kansas City Southern Ry. Co. v. United States,* 231 U.S. 423, 442 (1913).

FCC argued this point after its uniform system was promulgated in 1935. The uniform system was attacked by a number of telephone companies that were concerned that amounts included in certain accounts, reflecting the difference between the "original cost" of assets and their cost of acquisition to the reporting utility, would be written off. The FCC assured this Court, however, that the reporting of plant costs would not necessarily determine their disposition.[21]

Consistent with the assurances given this Court, the FCC has never regarded the accounting reports as binding even for its own ratemaking. In 1956, when it approved changes in the accounting for certain operating expenses, the FCC stated that the proceeding involved "accounting, not rate making."[22] It added: "[W]e do not intend that this document should be construed as setting forth any opinion concerning the rate-making aspects of the items at issue."[23] In 1979, in a decision that harmonized the ratemaking and accounting treatment of construction work, the FCC stated: "[I]t is well established that accounting prescriptions are, in general, not conclusive as to substantive rights and do not govern the treatment of an account for ratemaking purposes. . . ."[24] Likewise, State courts and agencies have repeatedly held that the FCC

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[21] *American Tel. & Tel. Co. v. United States,* 299 U.S. 232 (1936). *See also* Kripke, *A Case Study in the Relationship of Law and Accounting: Uniform Accounts 100.5 and 107,* 57 HARV. L. REV. 433, 450-51 (1944).

[22] *Amend. of Part 31,* 13 PUR3d 163, 167 (1956).

[23] *Id.* at 168.

[24] *American Tel. & Tel. Co.,* 72 F.C.C.2d 1, 5 (1979) (citations omitted).

uniform system of accounts is not determinative for ratemaking.[25]

State agencies often make ratemaking adjustments to the data reported pursuant to the FCC uniform system. The following adjustments are common, although they differ from uniform accounting prescriptions:

1) Capitalization of interest on short-term construction;
2) Capitalization of research and development costs;
3) Adjustment of depreciation rates;
4) Adjustment of expenses reported by companies, especially those resulting from affiliated transactions.[26]

The FCC has always been aware that many differences exist between its own accounting policies and the ratemaking practices of State agencies. Thus, when the FCC changed its uniform system in 1978 to authorize current earnings on short-term construction work, it stated:

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[25] *E.g., South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 352 So.2d 964, 981 (La. 1977), *cert. denied,* 437 U.S. 911 (1978); *Citizens v. Florida Pub. Serv. Com'n,* 415 So.2d 1268 (Fla. 1982); *see Washington Pub. Int. Org. v. Public Serv. Com'n,* 393 A.2d 71, 80 (D.C. App. 1978), *cert. denied,* 444 U. S. 926 (1979).

[26] *See State ex rel Southwestern Bell Tel. Co. v. Public Serv. Com'n,* 645 S.W.2d 44, 52-54 (Mo.App. 1983) (short term construction); *South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 352 So.2d 964, 981 (La. 1977), *cert. denied,* 437 U.S. 911 (1978) (research and development); *Pacific Tel. & Tel. Co. v. Public Util. Com'n,* 401 P. 2d 353, 372-73 (Cal. 1965) (depreciation); *South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 373 So.2d 478, 487 (La. 1979) (expenses).

"We do not believe, nor is it intended, that the accounting changes adopted in this proceeding impinge upon the ratemaking prerogatives of any state commission. Further, as everyone is aware, different treatment is already given to a number of items for intrastate vs. interstate ratemaking . . . ."[27]

To the extent possible, the State agencies avoid requiring duplicative records.[28] Nevertheless, when ratemaking adjustments are made to accounts of utilities, separate records are often required to facilitate intrastate ratemaking. In some states, such as New York, the regulatory agency prescribes its own system of accounts.[29] The FCC has always acknowledged the need for separate intrastate records. When the FCC adopted its first uniform system of accounts in 1935, its order provided:

> Nothing herein contained shall be construed as prohibiting or excusing any such carrier . . . from subdividing the accounts herein prescribed in the manner ordered by any State commission having jurisdiction or to the extent necessary to secure the information required in the prescribed reports to such commissions.[30]

In 1941, the FCC incorporated a virtually identical provision in its regulations.[31] This provision remains in the Code to this day.

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[27] *Amend. of Part 31*, 68 F.C.C.2d 902, 906 (1978).

[28] Kripke, *supra* n.21 at 438 n.22 (1944).

[29] *See, e.g., Re Accounting Treatment*, 71 PUR3d 440 (N.Y.P.S.C. 1967); 16 N.Y.C.R.R. §660 *et. seq.* Wisconsin also has its own accounting system.

[30] *Accounting Rules for Telephone Companies*, 1 F.C.C. 45, 46 (1935) (Order No. 7-C).

[31] 47 C.F.R 31.01-2(f).

Under the FCC-prescribed uniform system of accounts, companies report their plant and expenses on a combined basis. Intrastate records are developed using the separations process to reflect intrastate operations.[32] To the extent that State ratemaking laws, regulations or requirements differ from accounting policies, and special records are needed for intrastate ratemaking, these subaccounts become part of the intrastate records.[33]

The 1935 uniform system of the FCC contained accounts for depreciation expense and accumulated depreciation, as well as instructions for developing depreciation rates. However, the FCC did not actively enforce its depreciation instructions on interstate plant until the 1940s. During that time, the States were exercising their authority to prescribe depreciation accrual rates for intrastate plant. After the FCC began exercising its authority, both the FCC and the States prescribed depreciation rates for their respective jurisdictions. In an effort to achieve uniformity, the FCC, State commissions and carriers began conducting three-way meetings to negotiate the depreciation rates for each State.[34] Agreements normally have been reached, but because the rates were negotiated, they nearly always have varied from State to State, even for the same company.[35]

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[32] *See* 47 C.F.R. Part 67 (1984).

[33] In States with their own uniform accounting systems, the State records are not really subaccounts, but separate State accounts.

[34] *See Prescription of Revised Percentages of Depreciation*, 88 F.C.C.2d 1223, 1225, 1230-31 (1982).

[35] *Id.* at 1248-1301.

When agreements have not been reached, the State agencies have used State-prescribed depreciation practices for intrastate ratemaking and carriers have maintained separate depreciation records pursuant to these practices.[36]

3. FCC proceedings below.

The FCC issued two orders in 1980 and 1981 to modify the accounting practices prescribed for carriers. In 1980, it amended 47 C.F.R. §31.02-80 to authorize carriers to begin using the "equal life group"and "remaining life" procedures in developing depreciation rates rather than the traditional "vintage group" and "whole life" procedures ("*Depreciation Order*").[37]

The *Depreciation Order* acknowledged that depreciation measures are inherently imprecise and require the exercise of judgment,[38] and that the issues are "complex and not readily characterized as 'right' or 'wrong.' "[39] In approving the equal life group method, the FCC permitted the new method *at the option of the carrier.*[40] The change to the remaining life method was also made optional.[41] The new depreciation methods allowed carriers to record increased depreciation expense on their accounts.

In 1981, the FCC modified the accounting method for station connection costs, requiring the expensing of these costs rather than the traditional capitalization

[36] *See, e.g., Pacific Tel. & Tel. Co. v. Public Util. Com'n,* 401 P.2d 353, 372-73 (Cal. 1965).

[37] *Amend. of Part 31,* 83 F.C.C.2d 267 (1980).

[38] 83 F.C.C.2d at 271, 280.

[39] *Id.* at 280.

[40] *Id.*

[41] *Id.* at 290.

costs rather than the traditional capitalization and depreciation of the expenditures ("*Expensing Order*").[42] This change is similar to the earlier ruling permitting the expensing rather than capitalization of interest on short-term construction.[43]

After the issuance of the *Expensing Order,* petitions were filed with the FCC seeking a clarification that it was not binding on State agencies for intrastate ratemaking.[44] The FCC responded with a decision that "state commissions are not precluded from using their own accounting and depreciation procedures for intrastate ratemaking purpose[s] . . . ."[45] It concluded that Section 220 of the Communications Act does not require State agencies to adhere to FCC-prescribed accounting and depreciation methods. It also ruled that preemption was not necessary to further any Federal policy. The FCC specifically noted that "[m]any states have adopted different accounting practices for intrastate ratemaking than those prescribed by the uniform system."[46]

The FCC reversed itself in its *Preemption Decision.*[47] Acting on petitions filed by telephone carriers, it determined that Section 220(b) of the Communications Act, which required the FCC to prescribe depreciation practices for carriers, precludes the States from departing from FCC depreciation rates in fixing intrastate rates.[48] In reaching its decision, the FCC characterized its *Expensing*

[42] *Amend. of Part 31,* 85 F.C.C.2d 818 (1981).

[43] *Amend. of Part 31,* 68 F.C.C.2d 902 (1978).

[44] *Amend. of Part 31,* 89 F.C.C.2d 1094 (1982), J.S. App. at A-61.

[45] *Id.* at 1095, J.S. App. at A-62.

[46] *Id.* at 1108-09, 1108 n.19, J.S. App. at A-84, A-81 - A-82 n.19.

[47] 92 F.C.C.2d 864 (1983), J.S. App. at A-24.

[48] *See Preemption Decision,* 92 F.C.C.2d at 879, J.S. App. at A-49.

Order as a depreciation decision. Although this ruling required the expensing rather than capitalization of station connection costs, the FCC called it a depreciation ruling because the plant would no longer be depreciable.[49] The FCC did not distinguish prior decisions permitting the expensing rather than capitalization of costs. For example, in its decision on short-term construction work, the FCC disclaimed any intent to bind intrastate ratemakers.[50]

Alternatively, the FCC determined that it would preempt inconsistent State depreciation practices under its general power to further a Federal policy.[51] The FCC concluded that it was necessary to preclude *any* State from applying inconsistent depreciation policies to any plant for intrastate ratemaking.

The Federal "policy" identified by the FCC as served by preemption was a need for faster capital recovery in a "competitive environment" to encourage innovation and better allow carriers "to fully compete in the continually evolving telecommunications marketplace."[52] The alleged analysis of the impact on competition consisted of a series of speculations as to possible consequences of inconsistent State practices. The FCC found that slower capital recovery "could delay or prevent" modernization.[53] It also found that slower capital recovery "could well impair" capital attraction, which then "could undermine" the objective of developing an efficient telecommunications

[49]*Id.* at 868, J.S. App. at A-30 - A-31.

[50]*Amend. of Part 31,* 68 F.C.C.2d 902 (1978).

[51]*Preemption Decision,* 92 F.C.C.2d at 875-78, J.S. App. at A-42 - A-48.

[52]*Id.* at 877, J.S. App. at A-45 - A-46.

[53]*Id.*

market place.[54] The FCC made no empirical analysis quantifying, or even approximating, the effect of its new accounting methods on capital recovery.[57] Nor did the FCC explain why local exchange carriers providing monopoly services, subject to regulation, should be provided capital recovery permitting them to "compete" in the "telecommunications marketplace."[56]

The *Preemption Decision* voided State depreciation rates, policies and accounting practices different from those that carriers were permitted to adopt pursuant to the *Depreciation Order* and *Expensing Order.*[57] The FCC also indicated a belief that *all* Federal accounting and depreciation policies are preemptive.[58] It said: "[W]e will not allow inconsistent accounting or depreciation methods unless such practices are otherwise consistent with the public interest."[59]

The *Preemption Decision* allows carriers to record higher expenses for the expensing of station connections and faster depreciation in many States, and precludes State commissions from adjusting the accounts for intrastate ratemaking. Rate increases are therefore required to match the increased expenses, at least in States where

[54]*Id.* at 877, J.S. App. at A-46.

[55]*See Preemption Decision,* 92 F.C.C.2d at 876-78, J.S. App. at A-46 -A-48.

[56]*See Preemption Decision,* 92 F.C.C.2d at 877, J.S. App. at A-46.

[57]*Id.* at 879, J.S. App. at A-49.

[58]*Id.* at 873-74, J.S. App. at A-39 -A-40.

[59]*Id.* at 873-74, J.S. App. at A-40.

faster capital recovery had not already been allowed.[60] In a number of Federal court enforcement proceedings, the States have been required to grant rate increases to comply with the ruling.[61]

4. Ruling of the court of appeals.

A petition for review of the *Preemption Decision* was filed by the Virginia State Corporation Commission in the court of appeals.[62] A number of States, State regulatory agencies and consumer advocates intervened in support of the petitioner. The court of appeals declined to decide whether the language of the Communications Act requires preemption.[63] Instead, in a 2-1 decision, it ruled that the "regulatory action" of the FCC was justified as "within its authority to ensure efficient operation of the interstate telephone network."[64]

Although the court of appeals recognized that Sections 152(b) and 221(b) of the Communications Act "reserve to the states the authority to prescribe rates for intrastate telephone service,"[65] it determined that these provisions are outweighed by the "primary emphasis upon

[60]In states such as Florida, which have rejected FCC depreciation policy but have other, more generous depreciation policies than the FCC, the affected carriers have not chosen to enforce the *Preemption Decision.*

[61]*E.g., South Central Bell Telephone Co. v. Louisiana Pub. Serv. Com'n.*, 744 F.2d 1107 (5th Cir. 1984); *appeal docketed*, No. 84-870 (U.S., Nov. 30, 1984).

[62]*Virginia State Corp. Com'n v. F.C.C.*, 737 F.2d 388 (4th Cir. 1984), J.S. App. at A-1.

[63]*Id.* at 392, J.S. App. at A-8.

[64]*Id.* at 394, J.S. App. at A-11.

[65]*Id.* at 392, J.S. App. at A-8.

a 'rapid, efficient, Nationwide, and world-wide' communication service."[66] According to the court, this "overriding concern,"[67] which is contained in the "purpose"[68] section of the Communications Act, permits the FCC to override the specific statutory reservation of power to the States.

The court of appeals employed a two-step analysis, based on *Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta*,[69] in approving preemption. First, it found that the FCC intended to preempt.[70] Second, it found that since the FCC is authorized by Section 220(b) to prescribe depreciation rates, the FCC acted within its power in requiring the States to raise intrastate rates for increased depreciation.[71] In applying the two-step analysis, the court of appeals gave no weight to the statutory provisions reserving ratemaking power to the States. The court of appeals accepted, without scrutiny, the FCC contention that "improper capital recovery does pose a true threat in today's competitive market."[72]

Judge Widener, in dissent, determined that the FCC and the majority had "effectively written 47 U.S.C. §§152(b) and 221(b) out of the Communications Act."[73] He added: "The logical result of this decision is to permit the

[66]*Id.*

[67]*Id.*

[68]47 U.S.C. §151, J.S. App. at A-131.

[69]458 U.S. 141 (1982).

[70]737 F.2d at 393-94, J.S. App. at A-11.

[71]*Id.* at 394, J.S. App. at A-11.

[72]*Id.* at 394, J.S. App. at A-12.

[73]*Id.* at 398, J.S. App. at A-21.

FCC to abrogate completely the state regulation of intrastate ratemaking for the carriers' intrastate operations in violation of the Communications Act."[74] The dissenting judge also observed that the asserted "threat" to competition was mere "theorizing."[75] He noted that the FCC had failed to show the relationship between the capital recovery of regulated monopoly carriers and the competitive abilities of unregulated carriers.[76]

The *Preemption Decision* was interpreted by the United States Court of Appeals for the Fifth Circuit in a proceeding to enforce the FCC ruling.[77] The court upheld an injunction requiring a dollar-specific intrastate rate increase and precluding the Louisiana Commission from adjusting a previously authorized rate of return. The court stated that the "Preemption Order comes perilously close to undermining completely state authority and discretion to set intrastate rates . . . ."[78]

The *Preemption Decision* had a significant impact on intrastate rates. The Louisiana Commission, for instance, was required in the enforcement proceeding to raise intrastate rates by more than $40 million to comply with the decision.[79] In its most recent rate order involving South

[74]*Id.* at 398, J.S. App. at A-22.

[75]*Id.* at 398, J.S. App. at A-20.

[76]*Id.* at 398, J.S. App. at A-20 - 21.

[77]*South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 744 F.2d 1107 (5th Cir. 1984).

[78]*Id.* at 1121.

[79]*South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n,* 570 F. Supp. 227 (M.D. La. 1983); *aff'd* 744 F.2d 1107 (5th Cir. 1984).

Central Bell Telephone Company, the Louisiana Commission determined that the *Preemption Decision* required $62.7 million of the total increase in revenues for the company.[80] If the *Preemption Decision* were implemented in Ohio in 1985, the impact on rates charged by the three major telephone companies could be as much as $64 million annually.[81]

The Florida Commission has rejected the equal life group method but nevertheless permits equivalent capital recovery to that prescribed by the FCC. Ironically, since no carrier chooses to enforce the FCC method, Florida depreciation for the present is based on the intrastate ratemaking practice.

ARGUMENT

Summary of the Argument

1. The ruling of the court of appeals approves the conscription of State regulatory officials to raise intrastate telephone rates. The decision is based on an incorrect interpretation of *Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta*[82] and other preemption decisions of this Court. The analysis of the court of appeals focused on language describing the general purpose of the Communications Act, but gave no weight to provisions reserving intrastate ratemaking to the States. The ruling permits a Federal agency, in pursuit of an agency-created "policy," to override statutory boundary lines and, without authority, displace State law.

2. The *Preemption Decision* requires rate increases to

[80]*Ex parte South Cent. Bell Tel. Co.,* Order No. U-15995-A (La. P.S.C., 1984), J.S. App. at A-112, A-120.

[81]*Re General Tel. Co. of Ohio,* No. 84-1026-TP-AIR (P.U.C. Ohio); *Re Cincinnati Bell Tel. Co.,* No.84-1272-TP-AIR (P.U.C. Ohio); *Re Ohio Bell Tel. Co.,* No. 84-1435-TP-AIR (P.U.C. Ohio).

[82]458 U.S. 141 (1982).

comport with the new FCC accounting and depreciation policies. Therefore, it conflicts with explicit provisions of the Communications Act. The Act limits the reach of FCC jurisdiction to interstate communications and grants autonomy to the States in regulating intrastate communications. The statute contemplates the separation of the interstate and intrastate plant and expenses of telephone carriers for regulatory purposes. It also recognizes that separate records may be necessary for intrastate accounting and ratemaking. By requiring State agencies to increase rates to conform with Federal accounting and depreciation practices, the FCC has undertaken an unauthorized foray beyond its regulatory jurisdiction and has entered a province reserved to the States by Congress.

3. Section 220 of the Communications Act, which permits the FCC to prescribe a system of accounts for telephone carriers, does not authorize the FCC to order intrastate rate increases. Section 220 was intended to foster uniform *reporting* of the affairs of carriers; it does not require uniform ratemaking. The FCC never previously viewed its accounting prescriptions as binding on the States, or even on itself, for ratemaking. Courts and regulatory agencies have consistently held that uniform accounting practices do not control ratemaking. No basis exists for the attempt by the FCC to transform a *reporting* provision into authority for setting intrastate rates.

4. The legislative history of the Communications Act confirms that Congress intended to preclude the FCC from engaging in intrastate ratemaking. The sponsors of the Communications Act repeatedly stated their intent to preserve State ratemaking autonomy. Congress rejected a version of Section 220(j) that implied that the States were denied the power to prescribe rates. Congress also decided not to include a version specifically reserving State authority, but this section was unnecessary. Ratemaking jurisdiction had already been reserved to the States. In the

final version of Section 220(j), Congress retained the prerogative to enact legislation to harmonize interstate and intrastate accounting. It thus denied the FCC the discretion to preempt State practices.

In addition, five decades of administrative practice confirm the Congressional intent to preserve State ratemaking autonomy. The plant and expenses of carriers have been divided, for ratemaking, in the separations process. The States have always been free to adjust data reported on the accounts of carriers for ratemaking, and dual records, including dual depreciation accounts, have been maintained for decades by carriers to facilitate ratemaking adjustments.

5. Since State ratemaking authority is protected by a federal statute, the only conceivable rationale for approving preemption would be the impossibility of reconciling the limiting provisions with other statutory provisions. The impossibility rationale was the underlying basis for past decisions of lower courts approving preemption by the FCC in other contexts. In this case, it is possible to divide ratemaking responsibilities and they have been divided for decades using the separations process. The division follows the Congressional plan. In addition, the so-called "conflict" identified by the FCC is based wholly on speculation and could not provide a valid basis for ignoring Congressional intent.

6. The Court has jurisdiction of the appeal taken by the Louisiana Commission pursuant to 28 U.S.C. §1254(2), which permits appeals to the Court when State laws are invalidated on Federal constitutional grounds. The decision of the court of appeals affirmed a ruling that invalidates State ratemaking orders, which are considered statutes for the purpose of 28 U.S.C. §1254(2). Therefore, the Court should find that its appellate jurisdiction was properly invoked.

I. THE *PREEMPTION DECISION* IMPROPERLY SUBVERTS THE INTENT OF CONGRESS TO PRESERVE STATE AUTHORITY OVER INTRASTATE TELEPHONE COMMUNICATIONS.

In mandating that State regulators increase intrastate telephone rates to conform to Federal accounting prescriptions, the FCC invaded the authority reserved to the States in the Communications Act. In the statute, Congress expressly prohibited the FCC from regulating intrastate telephone communications and, particularly, intrastate rates. The legislative history and five decades of administrative practice confirm this Congressional intent. Section 220 of the Act. which is a reporting rather than a ratemaking provision, provides no support for the FCC action. Since the separations process provides for the coexistence of Federal and State ratemaking practices, there is no "impossibility" argument for reading away the provisions protecting intrastate authority. Therefore, the *Preemption Decision* is invalid.

The court of appeals purportedly applied the preemption standard announced by this Court in *Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta*[83] in upholding the *Preemption Decision.* The *de la Cuesta* test for preemption is: first, whether the agency intended to preempt state law; and, second, whether the agency action was within the scope of the agency's delegated authority.[84] However, in mechanically applying this Court's two-part test, the court of appeals ignored the restrictions on FCC jurisdiction contained in the Communications Act, contrary to *de la Cuesta.* Indeed, this Court reaffirmed that the agency must respect boundary lines set by Congress. It held that a

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[83]458 U.S. 141 (1982).

[84]*Id.* at 154.

preemptive decision should be overruled when " 'it appears from the statute or its legislative history that the [preemption] is not one that Congress would have sanctioned' "[85] or when it is " 'inconsistent with' "[86] the underlying statute. To determine whether the agency had discretion to act as it did, the Court in *de la Cuesta* reviewed the language and legislative history of the statute in question.[87]

Here, the court of appeals was not faithful to this analysis. With respect to the first part of the *de la Cuesta* test, it correctly found that the FCC intended to preempt.[88] With respect to the second part, the court accepted, without question, the FCC's assertion that its action was authorized because it was necessary to further a federal policy.[89] The court of appeals focused on general "purpose" language in the Act, but refused to give meaning to sections preserving State jurisdiction. It also ignored the legislative history of the Act and nearly fifty years of practice. The court found the *Preemption Decision* permissible based on this faulty analysis. The ruling of the court of appeals is deficient because *de la Cuesta* requires respect for Congressional boundary lines.

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[85]*Id.*, quoting *United States v. Shimer,* 367 U.S. 374, 383 (1961).

[86]*Id.*, quoting *Free v. Bland,* 369 U.S. 663, 668 (1962).

[87]*Id.* at 159 *et seq.*

[88]737 F.2d at 393, J.S. App. at A-9 - A-10.

[89]*Id.* at 395, J. S. App. at A-12 - A-14.

A. The FCC Requirement that State Agencies Increase Intrastate Telephone Rates is Contrary to the Express Statutory Reservation of Intrastate Authority to the States.

The Communications Act specifically precludes the FCC from regulating any aspect of intrastate telephone communication. Section 2(b) of the Act is a broad provision reserving State authority:

> *[N]othing* in this chapter shall be construed to apply or to give the commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier . . . .[90]

This language preserves the authority of State agencies over all intrastate charges and intrastate ratemaking practices. Since it appears in the section entitled "APPLICATION OF ACT," it controls all of the provisions granting affirmative authority to the FCC. This provision is the cornerstone of a detailed Congressional plan for dividing Federal and State regulatory authority.[91]

In addition, Congress chose to permit State regulation of certain aspects of interstate communication. Section 3(e), which defines "[i]nterstate communication" and "interstate transmission," and therefore determines that reach of FCC power,[92] states that these terms "shall not . . . include wire or radio communication between points

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[90]47 U.S.C. §152(b), J.S. App. at A-132 *(emphasis added)*.

[91]*See* 47 U.S.C. §§203(a), 213(h), 214(a) and 221(a), (c), (d). *See also* 47 U.S.C. §§153(r), (u).

[92]*See* 47 U.S.C. §§151, 152(a), J.S. App. at A-131.

in the same State . . . through any place outside thereof, if such communication is regulated by a State commission."[93] Section 221(b) also reserves jurisdiction to the States over exchange service "subject to regulation by a State commission or by local governmental authority," even when a "portion of such exchange service constitutes interstate or foreign communication."[94]

These provisions establish a clear intent to separate the interstate and intrastate regulatory jurisdictions, and preclude the FCC from regulating intrastate rates. Yet the *Preemption Decision*, when enforced by carriers, requires State regulators to adjust intrastate rates. Since the FCC ruling contravenes the Communications Act, it is not within the preemptive power delegated to the agency.

The *Preemption Decision* runs counter to the statutory provisions for the separation of interstate and intrastate telephone plant and expenses for ratemaking. These provisions provide an administrative mechanism for implementing the separations principle announced by this Court in *Smith v. Illinois Bell Tel. Co.*[95] Section 221(c) of the Act provides that the FCC may "determine what property of [a carrier] shall be considered as used in interstate or foreign telephone toll service."[96] Section 410(c), passed in 1971, provides for joint board proceedings to develop separations procedures.[97] As the Senate Report on the

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[93]47 U.S.C. §153(e), J.S. App. at A-132 - A-133.

[94]47 U.S.C. §221(b), J.S. App. at A-136 - A-137.

[95]282 U.S. 133 (1930).

[96]47 U.S.C. §221(c), J.S. App. at A-137.

[97]47 U.S.C. §410(c), J.S. App. at A-138 - A-139.

1971 Act stated, the "allocations must be reasonable, i.e., the rate base for each jurisdiction must have appropriate correlation to the different uses of the commonly used plant."[98] Thus, the statute contemplates that the separations process will determine the limits of Federal and State ratemaking jurisdiction pursuant to the mandate of *Illinois Bell*.[99] The *Preemption Decision* violates this division of authority.

The decision of the court of appeals is also contrary to Section 410(b) of the Communications Act, in which Congress expressly contemplated that State commissions would maintain separate records from those of the FCC for ratemaking.[100] This section provides that the Commission may confer with State commissions concerning the relationship of Federal and State rate structures, accounts, practices and classifications and may avail itself of records provided by State commissions. If Congress had intended that only the FCC could require record keeping by telephone carriers, this provision would not have been included in the Act.

The court of appeals circumvented the provisions preserving State authority by focusing primarily on general "purpose" language in Section 151 of the Act. This approach violates established principles of statutory construction. The analysis must involve review of the statutory whole and not the selection of provisions out of context, so that "all parts of a statute, if possible, are to

[98]S. Rep. No. 92-632, 92d Cong., 1st Sess., *reprinted in* 1971 U.S. Code Cong. & Ad. News 1511, at 1512.

[99]282 U. S. at 149.

[100]47 U.S.C. §410(b), J.S. App. at A-138.

be given effect." *American Textile Mfr. Inst., Inc. v. Donovan*.[101] If an ambiguity appears to exist, each provision should be read as being in harmony with the others, so as not to create a conflict. *Washington Market Co. v. Hoffman*.[102] The provisions should not be read to render the statute partly ineffective or inefficient. *United States v. Powers*.[103]

Applying these principles, the court of appeals misapplied *de la Cuesta*. Congress may have established the general goal "to make available . . . a rapid, efficient, Nation-wide, and world-wide wire . . . communication service . . . ,"[104] but it enacted a dual regulatory system to achieve that goal, reserving intrastate jurisdiction to the States. The court's narrow focus on Section 151 eliminated boundary lines written into other sections. This approach is erroneous, because *de la Cuesta* does not suggest that a court may ignore limiting provisions in a statute.

Although the FCC and the court of appeals referred to Section 220(b) as supporting the *Preemption Decision*,[105] Section 220(b) and the other provisions of Section 220 merely permit the FCC to prescribe methods for *reporting* the financial affairs of carriers. They do not authorize

[101]452 U.S. 490, 513 (1981).

[102]101 U.S. 112 (1879).

[103]307 U.S. 214, 217 (1983).

[104]47 U.S.C. §151, J.S. App. at A-131.

[105]*Preemption Decision*, 92 F.C.C. 2d at 869-70, J.S. App. at A-31 - A-33; *Virginia State Corp. Com'n v. F.C.C.*, 737 F.2d 388, 394 (4th Cir. 1984), J.S. App. at A-11.

the FCC to set intrastate rates. Therefore, no statutory authorization supports the agency action.

Section 220 was based on Section 20 of the Interstate Commerce Act, which was passed because the accounting systems of carriers had not been uniform. As this Court stated in 1913 in upholding Section 20, Congress "manifested a purpose to standarize and render uniform the accounts of the different carriers." *Kansas City Southern Ry. Co. v. United States.*[106] Section 220 of the Communications Act also was a reporting provision. Indeed, when the FCC initially prescribed its uniform system of accounts pursuant to this section, it assured this Court that the reporting requirements would not necessarily determine the ultimate disposition of assets.[107] Since then, the FCC has consistently maintained that its accounting prescriptions are not binding for ratemaking.[108] As the FCC stated in 1979, it "is well established that accounting prescriptions . . . do not govern the treatment of an account for ratemaking purposes . . . ." [109] In its first ruling on the preemption issue, the FCC acknowledged that administrative agencies and courts uniformly held for four decades that Section 220 does not inhibit State ratemaking prerogatives.[110]

[106]231 U.S. 423, 442 (1913).

[107]*American Tel. & Tel. Co. v. United States,* 299 U.S. 232 (1936).

[108]*Amend. of Part 31,* 13 PUR3d 163, 167 (1956); *American Tel. & Tel. Co.,* 64 F.C.C.2d 1, 56-60, 62, 68 (1977).

[109]*American Tel. & Tel. Co.,* 72 F.C.C.2d 1, 5 (1979).

[110]*Amend. of Part 31,* 89 F.C.C.2d 1094, 1107 (1982), J.S. App. at A-83.

Decisions of State courts and administrative agencies consistently hold that the accounting provisions of the FCC are not binding for intrastate ratemaking. For instance, the District of Columbia Court of Appeals made an extensive analysis of the history of the Communications Act and determined that the uniform accounting system "merely was a system of notation, without substantive significance." *Washington Pub. Int. Org. v. Public Serv. Com'n.*[111] The court held that uniform accounting precepts of federal agencies are not binding for ratemaking. In addition, the Supreme Court of California ruled that the California Commission was "not bound by the depreciation rates or methods set by the Federal Communications Commission." *Pacific Tel. & Tel. Co. v. Public Util. Com'n.*[112]

The Louisiana Supreme Court also has held that the uniform accounts of the FCC are not binding. In upholding a decision to capitalize costs that were expensed under the uniform system, it said: "The fact that capitalization of research costs may not accord with accounting practices prescribed by the F.C.C. does not necessarily render it unreasonable." *South Cent. Bell Tel. Co. v. Louisiana Pub. Serv. Com'n.*[113] The conclusion that federal accounting precepts are not binding for intrastate ratemaking appears to be universally shared by state courts and regulatory agencies.[114]

[111]393 A.2d 71, 80 (D.C. App. 1978), *cert.denied,* 444 U.S. 926 (1979).

[112]401 P.2d 353, 372-73 (1965).

[113]352 So.2d 964, 981 (La. 1977), *cert. denied,* 437 U.S. 911 (1978).

[114]*New England Tel. & Tel. Co. v. Public Util. Com'n,* 448 A.2d 272, 293 (Maine 1982); *State ex rel Southwestern Bell Tel. Co. v. Public Serv. Com'n,* 645 S.W.2d 44, 54-56 (Mo.App. 1983); *Washington Util. and Transp. Com'n v. Pacific Northwest Bell Tel. Co.,* 39 PUR4th 126, 135-36 (Wash. U.T.C., 1980); *Southwestern Bell Tel. Co.,* 36 PUR4th 283, 294 (Mo. P.S.C., 1980); *Re Accounting Treatment,* 71 PUR3d 440, 442 (N.Y. P.S.C., 1967); *Southern Bell Tel. & Tel. Co.,* 66 PUR3d 1, 58 (Fla. P.S.C., 1966).

The federal courts of appeals have recognized the universal regulatory principle that accounting precepts cannot dictate ratemaking in reviewing decisions of the Federal Power Commission and its successor, the Federal Energy Regulatory Commission. In *Alabama-Tennessee Nat. Gas Co. v. F.P.C.*, the Fifth Circuit ruled that the FPC uniform system was a valuable tool, but it "cannot dictate ratemaking policies."[115] The District of Columbia Circuit and the Fourth Circuit have reached similar conclusions.[116]

Section 220 does not authorize the FCC to prescribe ratemaking practices for the States. This provision is designed to bring about uniform reporting, not uniform ratemaking. As a reporting provision, Section 220 is wholly consistent with the sections preserving State ratemaking jurisdiction, especially since Section 221(c) contemplates separation of interstate and intrastate plant for ratemaking and Section 410(b) recognizes that separate State records may be maintained to facilitate intrastate ratemaking.

The reliance on Section 220(b) is also unjustified because Section 220(j) precludes FCC discretion to preempt State depreciation and accounting. It directs the FCC to report to Congress on the need for legislation to harmonize State and Federal powers over accounting and depreciation. Thus, Congress reserved to itself, and denied the FCC, the power to change the relationship of Federal and State authority under Section 220.

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[115]359 F.2d 318, 336 (5th Cir. 1966).

[116]*Public Systems v. F.E.R.C.*, 606 F.2d 973, 982 (D.C. Cir. 1979) ("[D]espite the obvious relevance of accounting precepts for some regulatory policies, they cannot supply an independent basis for action when they may conflict with established ratemaking principles."); *Consolidated Gas Supply Corp. v. F.E.R.C.*, 653 F.2d 129, 135 (4th Cir. 1981). *See also* A.J.G. PRIEST, PRINCIPLES OF PUBLIC UTILITY REGULATION 611 (1969).

The use of the reporting authorization to force intrastate rate increases produces an especially egregious interference with intrastate prerogatives. Since carriers report *all* their investment and expenses using the FCC uniform system, their accounts include purely intrastate plant, as well as the intrastate portion of jointly used plant. The *Preemption Decision* requires the use of the FCC depreciation methods for ratemaking even with respect to the purely intrastate plant.

The FCC decision to delegate to carriers the right to preempt State ratemaking adds an ironic twist to the subversion of Congressional intent. By giving carriers the option of adopting faster depreciation methods in the *Depreciation Order*, then preempting inconsistent State rules, the FCC allowed the carriers to decide whether State depreciation practices are displaced. This assignment of preemptive power permits the carriers to dictate to State regulators — a result that Congress did not intend. Even if the FCC had preemptive power, the Communications Act does not permit its delegation to the regulated telephone companies.[117]

The cavalier treatment of specific statutory limits by the court of appeals obliterates a premise of preemption theory. In *Garcia v. San Antonio Met. Transit Auth.*,[118] this Court examined affirmative limits on Congressional power under the Commerce Clause.[119] It found that "the principal and basic limit on the federal commerce power is

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[117]*Cf. Greene County Plan. Bd. v. F.P.C.*, 455 F.2d 412, 420 (D.C. Cir. 1972), *cert. denied*, 409 U.S. 849 (1972).

[118]105 S.Ct. 1005 (1985).

[119]U. S. Const. art. I, §8.

that inherent in all congressional action — the built-in restraints that our system provides through state participation in federal governmental action."[120] Thus, a true implementation of Congressional intent is critical in order to afford States the procedural safeguards upon which *Garcia* rests. If the FCC is permitted to read away limiting provisions of the Act, then the basic safeguard for State authority has been eliminated.

The *Preemption Decision* is an unauthorized usurpation of the authority reserved by Congress to the States. Congress contemplated that Federal and State ratemaking authority would be divided using the separations process, and that the FCC should not invade the intrastate realm. The Act contains no affirmative authority for overriding the Congressional scheme. Therefore, the ruling should be reversed.

B. The Legislative History of the Communications Act and the History of Its Implementation Confirm Congressional Intent to Limit the Jurisdiction of the FCC and Preserve State Autonomy Over Intrastate Communications.

In preemption cases the Court has looked to legislative history to determine the intent of Congress.[121] Had the court of appeals analyzed the legislative history, this review would have shown that Congress intended to preclude the FCC from engaging in intrastate ratemaking.

[120] 105 S.Ct. at 1020.

[121] *Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 163-67 (1982).

The legislative history of the Communications Act of 1934 demonstrates that Congress had a clear, unequivocal intent to limit FCC authority and preserve State autonomy over intrastate communications. Indeed, the foremost concern of Congress in enacting Title II of the Act was the division of Federal and State authority. This one aspect of telephone regulation received more attention than any other during hearings, in reports and during floor debates. With respect to Section 220, the legislative history demonstrates that Congress did not intend to preempt State authority over accounting or depreciation rates. It intended that any conflict between Federal and State authority be resolved by legislation. Fifty years of administrative practice, in which FCC accounting practices were never seen as binding for intrastate ratemaking, confirm the workability of the Congressional plan.

Bills introduced in both the House and Senate contained provisions limiting FCC authority and preserving State autonomy over intrastate communications.[122] These provisions were apparently drafted with the aid of representatives of State regulatory agencies.[123] The central limiting provisions were ultimately enacted as Sections 2(b) and 221(b) of the Act. These sections reserve to the States all authority to regulate intrastate communications and were strongly supported during committee hearings.

[122] The bills were designated S. 2910 and H.R. 8301. The limiting provisions in S. 2910 were contained in sections 2, 3(e), 210, 220(j) and 221(a)(b)(c) & (d). The limiting provisions in H.R. 8301 were contained in Sections 2, 3(e), 210, 214(e), 220(j) and 221(a)(b)(c) & (d).

[123] See statement of Chairman Dill, Hearings on S. 2910 before the Senate Committee on Interstate Commerce, 73d Cong., 2d Sess. ("Sen. Comm. Hearings") at 179 (1934).

Representatives of the National Association of Railroad and Utility Commissioners ("NARUC") appeared on behalf of State regulatory agencies and urged passage of the bills with the limiting language intact.[124] The States were concerned that a new commission would effectively eliminate meaningful regulation by the States, if it exerted the broad authority of the ICC without limiting provisions.

NARUC emphasized that the States were not wedded to any specific language, but advocated language that would prevent their authority from being eroded.[125] The independent telephone companies supported the provisions limiting FCC authority and, in addition, proposed that local telephone companies carrying interstate calls only via connection to the Bell network, be exempted from FCC authority.[126]

There was little controversy over the proposed division of Federal and State authority. AT&T briefly urged a simple transfer of authority from the ICC to the new Commission.[127] The Senate Committee received suggestions that S. 2910 should be amended to expressly extend FCC authority to the entire communications network.[128] In written comments, a representative of the ICC advised

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124 *See* Statements of Messrs. Benton, Clardy and McDonald, Sen. Comm. Hearings at 153-155, 155-157 and 178-184; Hearings on H.R. 8301 before the House Committee on Interstate and Foreign Commerce, 73rd Cong., 2d Sess. ("H.R. Comm. Hearings"), at 70-74, 131-147 (1934).

125 Sen. Comm. Hearings at 154-55, 179-80; H.R. Comm. Hearings at 71, 73, 136, 132.

126 *See* comments of Messrs. MacKinnon, Derring, Hedreck, and McKinney, H.R. Comm. Hearings at 239, 241, 248, 252, 254 and 273.

127 *See* Sen. Comm. Hearings at 77, 213-16.

128 *See* Comments of Messrs. McDonough and Nockels, Sen. Comm. Hearings at 114-16, 199.

that subsection 221(b) might result in ineffective interstate regulation.[129] However, both committees and, ultimately, both houses of Congress agreed to the division of Federal and State authority as proposed and adopted provisions that further limited FCC authority.

The Senate Committee on Interstate Commerce endorsed the division of Federal and State authority and rejected the simple transfer of authority from the ICC.[130] Its report noted that Section 2 of the bill reserved exclusive State jurisdiction over intrastate communication.[131] On the Senate floor, Senator Dill emphasized that the bill *preserved* State authority to regulate intrastate communications.[132]

The House report also endorsed the division of Federal and State authority in H.R. 8301.[133] Among other things, the House report noted that subsection 2(b) exempts the intrastate business of any carrier.[134] On the House floor, Representative Rayburn noted that the bill preserved State authority over intrastate communications.[135] H.R. 8301 was passed by the House without amendment as a substitute for S. 3285.[136]

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129 Sen. Comm. Hearings at 209, H.R. Comm. Hearings at 97.

130 S.Rep. No. 781, 73rd Cong., 2d Sess., at 1-2 (1934) ("S.Rep."). The report proposed to substitute S. 3285 in favor of S. 2910, but retained the division of authority in S. 2910.

131 S.Rep. at 3.

132 78 Cong. Rec. 8823 (1934).

133 *Id.* at 8846. One amendment changed subsection 2(h) to further exempt local companies that carried interstate calls only by connection to carriers with which they were not affiliated.

134 H.R. Rep. No. 1850, 73rd Cong., 2d Sess. (1934) ("H.R. Rep.").

136 78 Cong. Rec. 10313, 10314 (1934).

A conference committee was authorized to settle the differences between S. 3285 and H.R. 8301. As ultimately proposed by the conference committee and approved by each House, the Act contained ten provisions that limited FCC jurisdiction and preserved State autonomy over intrastate communications.[137]

Congress fully and carefully considered the scope of FCC authority and intended to limit FCC authority in favor of State autonomy over intrastate and local communication. The decision of the court of appeals flies in the face of the clear intent of Congress that the FCC could not preempt any State regulation of intrastate communication that simply affects an FCC interstate policy. Had Congress intended to permit the FCC to supercede State regulation, it would have simply transferred the ICC's power to the FCC. Instead, it explicitly preserved State autonomy.

Congress understood that State regulation would affect federal policy. That is the very basis of the *Shreveport Rate Case,* where intrastate rates were raised to the level prescribed by the ICC to avoid discrimination.[138] In enacting provisions to insulate State regulation and prevent a Federal determination of intrastate rates, Congress overruled the *Shreveport Rate Case.*[139] Congress' thoughtful, deliberate decision to permit a diverse array of regulatory policies belies any intent to permit preemption of State regulation to advance an agency policy.

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[137]These provisions were contained in subsections 2(b) (1), 2(b) (2), 3(e), 203(a), 213(h), 214(a) and 221(a)(b)(c) and (d).

[138]*Houston, E. & W. Texas Ry. v. United States,* 234 U.S. 342 (1914).

[139]*See North Carolina Util. Com'n v. F.C.C.,* 552 F. 2d 1036, 1047 (4th Cir.1977), *cert. denied,* 434 U.S. 874 (1977).

The *Preemption Decision* also conflicts with the legislative history of Section 220. As originally drafted, subsections (h)-(j) of Section 220 explicitly preserved State autonomy over systems of accounts and depreciation. NARUC endorsed subsection (j), which preserved State discretion to prescribe depreciation rates and forms of accounts, but did not urge adoption of its specific terms. The States sought language preserving their authority to obtain data needed for intrastate purposes and to review a carrier's depreciation rates when setting intrastate rates.[140]

AT&T vigorously attacked subsections (h) and (j). It urged that subsection (h) would permit the FCC to dismantle the existing uniform system of accounts and that subsection (j) would create an impossible situation for multistate companies.[141] AT&T never contended, however, that the States should be limited in their ability to obtain data or hindered in their intrastate ratemaking.[142] In written comments, a representative of the ICC advised that subsection (j) conflicted with the uniformity of systems of accounts and depreciation accounting required by subsection 220.[143]

NARUC, on the other hand, merely sought to ensure that the States could obtain data in addition to the FCC uniform system of accounts. It never endorsed multiple systems of accounts. In fact, it predicted that State participation under subsection (i) would lead to a uniform system that would fulfill many of the needs of the States. As far as depreciation was concerned, NARUC really only

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[140]H.R. Comm. Hearings at 138, 144, 143.

[141]*See* Sen. Comm. Hearings at 96, H.R. Comm. Hearings at 191.

[142]*See* comments of Walter S. Gifford, Sen. Comm. Hearings at 94-97; H.R. Comm. Hearings at 189-92.

[143]Sen. Comm Hearings at 208; H.R. Comm. Hearings at 96.

sought assurance that the States would remain unhindered in reviewing depreciation rates for intrastate ratemaking. The ICC had never prescribed depreciation rates for any telephone company. Instead, the individual States had been doing it, without any complaint from AT&T.[144]

In sum, AT&T sought uniform accounting and NARUC agreed to uniform accounting. Likewise, NARUC sought independent accounting and ratemaking authority and AT&T endorsed subaccounts which allow that. The States were reviewing depreciation rates and AT&T did not suggest that this practice should be prohibited.

The Senate rejected subsections (h) and (j) as drafted and amended those provisions to instruct the FCC to make further recommendations as to whether Congress should pass legislation to *permit* the State commissions to prescribe their own accounting and depreciation practices. On the other hand, the House retained the original language of subsections 220(h) and (j). The Conference Committee sided with the House on subsection (h) and rejected both versions of subsection (j) in favor of a modified version:

> The Commission shall investigate and report to Congress as to the need for legislation to define further or harmonize the powers of the Commission and of State Commissions with respect to matters to which this section relates.[145]

The final version of subsection (j) retains the Senate's direction that the FCC report on the need for legislation. However, it omits the language in the Senate's version suggesting that Section 220 preempts as a matter

[144]*See* H.R. Comm. Hearings at 140-44.

[145]47 U.S.C. §220(j), J.S. App. at A-136.

of law. Further, the section implies that the States may exercise "powers" with respect to accounting and depreciation. Had Congress intended to withhold State authority it would have adopted subsection (j) as passed by the Senate. Instead, the Conference Committee intended that State and Federal authority over accounting and depreciation be harmonized so that both interests could be preserved.

The Conference Committee had every reason to expect a harmonious exercise of FCC and State powers under a uniform system of accounts that accommodated the needs of the States. Subsection (i) required the FCC to receive and consider State commission comments, no doubt so that its uniform system would require data sought by the States or accommodate additional State requirements. Different accounting requirements, including different depreciation rates, could be accommodated in subaccounts. Nevertheless, since the system was as yet untried, subsection 220(j) directed the FCC to report on the need for legislation to further define or harmonize Federal and State powers over accounting and depreciation.

The intent of Congress to protect intrastate ratemaking authority is confirmed by almost 50 years of administrative practice. In implementing Section 220 of the Act, the FCC officially acknowledged and approved the practice of maintaining separate records for intrastate accounting and ratemaking.[146]Prior to the issuance of the *Preemption Decision,* the FCC had consistently acknowledged that its accounting provisions were not binding on the States for ratemaking.[147] The same conclusion

[146]*Accounting Rules for Telephone Companies,* 1 F.C.C. 45 (1935).

[147]*See supra* notes 107-10 and accompanying text.

was reached by State courts and agencies.[148] This history is strong evidence of Congressional intent, as this Court held in *BankAmerica Corp. v. United States.*[149]

This Court recognized that the failure of an agency to assert its authority is not determinative of the agency's lack of authority, but " 'failure to use such a power for a long time indicates to us that the commission did not believe the power existed.' "[150] When this non-exercise of power was combined with a consistent interpretation by informed agencies over an extended span that the power did not exist, the interpretation was given "powerful weight."[151]

The legislative history of the Federal-State Communications Joint Board Act, passed in 1971, shows that Congress was well aware of the historic development of dual regulation and the use of the separations process to define the limits of Federal and State ratemaking authority. The Senate Report on the Act states: "[F]or each jurisdiction effectively to exercise its authority, procedures are needed to apportion the costs for services under each jurisdiction."[152] Congress knew that the States prescribed ratemaking practices for plant allocated to intrastate jurisdictions. It implicity approved the continuation of this practice.

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[148]See *supra* notes 111-14 and accompanying text.

[149]103 S.Ct. 2266 (1983).

[150]*Id.* at 2272, quoting *Federal Power Com'n v. Panhandle Eastern Pipe Line Co.,* 337 U.S. 498, 513 (1949).

[151]103 S.Ct. 2272.

[152]S. Rep. No. 92-632, 92d Cong., 1st Sess., *reprinted in* 1971 U.S. Code Cong. & Ad. News 1511 at 1512.

The legislative history of the Communications Act, including Section 220, confirms the intent to preserve State ratemaking authority. Congress recognized that the States would require records for intrastate ratemaking and declined to withhold that authority. It reserved to itself — not to the FCC — the power to legislate further in the area. Fifty years of administrative history establish that the FCC never believed it could set intrastate rates. Therefore, the *Preemption Decision* conflicts with Congressional intent.

C. The Alleged Conflict Between the FCC Policy and State Law Does Not Justify the Evisceration of Statutory Limits on FCC Jurisdiction.

The FCC and the court of appeals referred to a conflict between the Federal policy and State laws and practices to justify the *Preemption Decision.*[153]In this respect, they misapplied the preemption analysis embodied in *de la Cuesta.* In that case, this Court analyzed whether a *valid* federal regulation could coexist with State provisions and, finding a conflict, invalidated the State practices.[154] A conflict analysis is not relevant, however, when Congress explicitly sanctions the exercise of State power.[154] In this case, the actual "conflict" is between an FCC policy and explicit limits contained in the Communications Act. The only conceivable rationale for reading out these limiting provisions would be the *impossibility* of reconciling *statutory* provisions.

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[153]*Preemption Decision,* 92 F.C.C.2d at 877, J.S. App. at A-95 - A-96; *Virginia State Corp. Com'n v. F.C.C.,* 737 F.2d at 395, J.S. App. at A-14 - A-15.

[154]*Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta,* 458 U.S. 141, 155-60 (1982).

The impossibility of dual regulation is, indeed, the underlying basis for the few lower court decisions finding that FCC regulations preempted conflicting State provisions. These rulings arose in circumstances not anticipated by Congress. The courts in these cases were faced with the task of reconciling Sections 152(a) and (b), which divide Federal and State regulatory authority. As the courts recognized, circumstances exist where this division is physically impossible. In these cases, either the FCC or the States must have exclusive authority. In each case, the courts determined that preemption was necessary because the continued existence of the intrastate regulations would curb the affirmative power of the FCC over interstate communications.

For instance, in *North Carolina Utilities Com'n v. F.C.C. ("NCUC"),*[156] the Federal and State tariffs contained conflicting provisions for the *physical* interconnection of jointly used equipment. Since the equipment could not be separated in the physical sense, reconciliation of the competing regulations was impossible. Similarly, in *Computer and Comm. Ind. Ass'n v. F.C.C.,*[157] the State laws and Federal regulations conflicted as to whether certain types of equipment could be regulated at all. The equipment could not be broken into its interstate and intrastate components, so the court approved preemption.

In contrast to the line of cases arising from *NCUC,* it is possible to accommodate the statutory provisions in this case. There is no conflict between the provisions allocating authority over the subject matter. Federal and

[156]537 F.2d 787 (4th Cir. 1976), *cert. denied,* 429 U.S. 1027 (1976).

[157]693 F.2d 198 (D.C. Cir. 1982), *cert. denied,* 461 U.S. 938 (1983).

State ratemaking responsibilities have been divided for decades through the separations process — a procedure mandated by this Court in *Smith v. Illinois Bell Tel. Co.*[158] and expressly sanctioned by Congress.[159] The court of appeals conceded that differing Federal and State accounting and ratemaking policies can coexist.[160] By intruding into the realm of intrastate ratemaking and requiring rate changes for plant allocated to the State jurisdiction, the FCC crossed a dividing line established by Congress.

Even if the FCC could overrule the division of authority in the Act by creating a new policy that conflicts with State law, it failed to demonstrate how its policy in this case will be furthered by the *Preemption Decision.* The asserted connection between the capital recovery of regulated, monopoly companies — which generally do not engage in competition — and effective competition in the telecommunications market place has never been established by the FCC and has no apparent logical basis. A mere eight months before the issuance of the *Preemption Decision,* the FCC had issued a well-reasoned analysis of the historical compatibility of simultaneous State and Federal regulation of the telephone industry. It concluded that there was no necessity to preempt.[161] Little weight should be given to the FCC's finding of a conflict in light of its abrupt reversal of position at the urging of regulated companies.

[158]282 U.S. 133 (1930).

[159]47 U.S.C. §§221(c), 410(c).

[160]737 F. 2d at 395, J.S. App. at A-15.

[161]*Amend. of Part 31,* 89 F.C.C.2d 1094 (1982), J.S. App. at A-61.

The decision of the court of appeals approves an attempt to rewrite the Communications Act. Moreover, the "purpose" analysis of the court of appeals is especially objectionable because it gives the FCC license to ignore all statutory limits to its authority over intrastate communication. If the FCC can preempt here under the aegis of Section 151, despite the specific reservation of State authority, then all ratemaking matters are open to FCC usurpation, as long as the issue arguably may foster the goals stated in Section 151.[162] But the FCC is bound by limits prescribed by Congress. As the court of appeals for the District of Columbia Circuit recently stated in a slightly different context, "we are not at liberty to release the agency from the tie that binds it to the text Congress enacted."[163] No matter how strongly the FCC desires to preempt State jurisdiction, Congress has not given it that authority and the FCC cannot assert what it does not have.

II. THIS COURT HAS APPELLATE JURISDICTION OF THE APPEAL PURSUANT TO 28 U.S.C. §1254(2).

This Court has jurisdiction over the decision of the court of appeals pursuant to 28 U.S.C. §1254(2), which permits appeals to this Court when State laws are invalidated as repugnant to the United States Constitution. The decision of the court of appeals affirmed a ruling that invalidates State ratemaking orders. The *Preemption Decision* has been interpreted in a Federal court enforcement proceeding as expressly invalidating ratemaking orders of the Louisiana Commission. The Federal court interpreted the decision as a "direct order . . . specifically declaring

[162]737 F.2d at 398, J.S. App. at A-21 (Widener, J., dissenting).

[163]*M.C.I. Telecomm. Corp. v. F.C.C.*, No. 85-1030 (D.C. Cir., July 9, 1985) at 4.

that inconsistent State prescribed depreciation rates are void."[164] The enforcement decision invalidated the State ratemaking orders on a constitutional ground: that they were preempted.[165]

Ratemaking orders of a legislative nature are State "statute[s]" for the purpose of 28 U.S.C. §1254(2).[166] Article 4, Section 21 of the Louisiana Constitution invests the Louisiana Commission with general regulatory authority over common carriers and public utilities. The ratemaking function of the Louisiana Commission is legislative.[167]

The *Preemption Decision* invalidates State laws on constitutional grounds. Congress intended that this Court have appellate jurisdiction to ensure that State laws are not deemed unconstitutional without review by the highest Federal court. Therefore, the Court has jurisdiction over the appeal of the Louisiana Commission. Alternatively, the Court should treat the appeal papers as a petition for certiorari pursuant to 28 U.S.C. §2103.

[164]*South Cent. Bell Tel. Co. v. Louisiana Public Serv. Com'n*, 570 F. Supp. 227, 236 (M.D.La. 1983), *aff'd* 744 F.2d 1107 (5th Cir. 1984).

[165]570 F.Supp. at 231-32; 744 F.2d at 1121.

[166]*E.g., Atchinson T. & S. F. Ry Co. v. Public Util. Com'n*, 346 U.S. 346, 348 (1953); *Lake Erie & Western R. Co. v. State Public Util. Com'n*, 249 U.S. 422, 424 (1919).

[167]*E.g., Gulf States Util. Co. v. Louisiana Pub. Serv. Com'n*, 364 So. 2d 1266, 1268 (La. 1978); *South Central Bell Tel. Co. v. Louisiana Pub. Serv. Com'n*, 352 So.2d 964, 969, (La. 1977), *cert. denied*, 437 U.S. 911 (1978).

CONCLUSION

The conscription of State regulatory officials to further a Federal policy by increasing intrastate telephone rates is unjustified. The *Preemption Decision* defies the express reservation of intrastate jurisdiction in the Communications Act, cuts deeply into the sovereignty of the States, and overturns more than five decades of regulatory precedent and practice. The preemption of State ratemaking practices is unnecessary because interstate and intrastate ratemaking functions are separable, and indeed have been separated for decades. Therefore, the Court should reverse the decision of the court of appeals, overturn the *Preemption Decision*, and reaffirm the autonomy of the States in setting intrastate telephone rates.

Respectfully submitted,

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